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No. 82-1565

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1983

BACCHUS IMPORTS, LTD., and EAGLE DISTRIBUTORS, INC.,
Appellants,

vs.

GEORGE FREITAS,
DIRECTOR OF TAXATION OF THE STATE OF HAWAII,
Appellee.

On Appeal from the Supreme Court of the State of Hawaii

OPENING BRIEF FOR APPELLANTS BACCHUS IMPORTS, LTD. AND EAGLE DISTRIBUTORS, INC.

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QUESTIONS PRESENTED

1. Does a state tax of 20% ad valorem on the sale at wholesale of all liquor sold in Hawaii, which singles out (by exemptions for locally produced liquors) imported liquor for discriminatory taxation, constitute a duty or impost on imports prohibited by the Import-Export Clause (U.S. Const. art. I, § 10, cl. 2)?

2. Does such a discriminatory state tax, imposed for the express purpose of fostering and protecting certain local liquor industries, and of promoting the consumption of their products, infringe unconstitutionally on the power of Congress under the Commerce Clause (U.S. Const. art. I, § 8, cl. 3)?

3. Does such a discriminatory state tax, by exempting from the tax certain locally made liquors while taxing similar liquors imported into Hawaii by appellant wholesalers, deny to them the equal protection of the laws (U.S. Const. amend. XIV, § 1)?*

******List of all parties to the proceedings below.* The parties to the proceedings in the Hawaii Tax Appeal Court and in the Hawaii Supreme Court were Bacchus Imports, Ltd. (plaintiff in Case No. 1852 in the tax appeal court), Eagle Distributors, Inc. (plaintiff in Case No. 1866), Paradise Beverages, Inc. (plaintiff in Case No. 1862), and Foremost-McKesson, Inc., dba McKesson Wine & Spirits Co. (plaintiff in Case No. 1867), and George Freitas, Director of Taxation of the State of Hawaii (defendant in all cases). In the Hawaii Supreme Court all of these cases were consolidated as No. 7802, October Term 1979.

Rule 28.1 statement. Appellants provided the list of parent companies, subsidiaries other than wholly-owned subsidiaries, and affiliates required by Rule 28.1 at page iii of their Jurisdictional Statement filed on March 15, 1983.

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OPINIONS BELOW

The opinion of the Hawaii Supreme Court in this case is reported at 65 Haw. ____, 656 P.2d 724 (1982), and is reproduced in the Appendix to the Jurisdictional Statement ("AJS") beginning at A-1. The opinion of the Hawaii Tax Appeal Court has not been reported, and is reproduced at AJS A-41.

JURISDICTION

The judgment of the Hawaii Supreme Court (AJS A-56), which sustained the validity of the Hawaii liquor tax (H.R.S. § 244-4, set out at pp. 2-3 *infra*) against a challenge based on the United States Constitution (art. I, § 8, cl. 3; art. I, § 10, cl. 2; and amend. XIV, § 1), was entered

on January 5, 1983. The notice of appeal (AJS A-59) was filed with the Hawaii Supreme Court on March 3, 1983 and the appeal was docketed on March 15, 1983. Probable jurisdiction was noted by this Court on June 20, 1983. The jurisdiction of this Court is invoked under 28 U.S.C. § 1257(2).

CONSTITUTIONAL AND STATUTORY PROVISIONS

Article I, section 8, clause 3 of the United States Constitution provides in part: "The Congress shall have power . . . [t]o regulate Commerce with foreign Nations, and among the several States . . . ."

Section 10, clause 2 of the same article provides in part: "No State shall, without the Consent of Congress, lay any Imposts or Duties on Imports or Exports . . . ."

Section 1 of the Fourteenth Amendment provides in part: ". . . No State shall . . . deny to any person within its jurisdiction the equal protection of the laws."

Section 2 of the Twenty-first Amendment provides: "The transportation or importation into any State, Territory, or possession of the United States for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited."

Section 244-4 of the Hawaii Revised Statutes, as amended to date, provides:

> Every person who sells or uses any liquor not taxable under this chapter in respect of the transaction by which such person or his vendor acquired such liquor, shall pay an excise tax which is hereby imposed, equal to twenty percent of the wholesale price of the liquor so sold or used, provided, that the tax shall be paid only once upon the same liquor; provided, further, that the tax shall not apply to:
>
> (1) Liquor held for sale by a permittee but not yet sold;
>
> (2) Liquor sold by one permittee to another permittee;

(3) Liquor which is neither delivered in the State nor to be used in the State, or which under the Constitution and laws of the United States cannot be legally subjected to the tax imposed by this chapter so long as and to the extent to which the State is without power to impose the tax;

(4) Liquor sold for sacramental purposes or the use of liquor for sacramental purposes, or any liquor imported pursuant to section 281-33;

(5) Alcohol sold pursuant to section 281-37 to a person holding a purchase permit or prescription therefor, or any sale or use of alcohol, so purchased, for other than beverage purposes;

(6) Okolehao manufactured in the State for the period May 17, 1971 to June 30, 1981;

(7) Any fruit wine manufactured in the State from products grown in the State for the period May 17, 1976 to June 30, 1981; or

(8) Rum manufactured in the State for the period May 17, 1981 to June 30, 1986.

STATEMENT OF THE CASE

This appeal presents a simple, but fundamental, question for review. May a state employ a tax which on its face discriminates against interstate and foreign commerce in order to foster and protect local industry? The surprising answer of the Hawaii Supreme Court was affirmative.

Appellants Bacchus Imports, Ltd. ("Bacchus") and Eagle Distributors, Inc. ("Eagle") are companies licensed to import alcoholic beverages into Hawaii and to sell them at wholesale to other licensees. Joint Appendix ("JA") 7, 12. Hawaii imposes a tax at a rate of 20% of the wholesale price on the first sale at wholesale of liquor.[1] Because the

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[1] "Liquor" is defined by section 281-1 of the Hawaii Revised Statutes as follows:

"Liquor" or "intoxicating liquor" includes alcohol, brandy, whiskey, rum, gin, okolehao, sake, beer, ale, porter, and wine;

tax is based on the actual wholesale price, it includes a tax on all freight charges, customs duties, and federal taxes, as well as the wholesaler's markup. JA 9-10, 16, 22-23. The tax is payable by the wholesaler whether or not it is collected from the purchaser, and is assessed on monthly gross sales reported to the state. JA 8-9, 15-16.

Over the years Hawaii's legislature has enacted several exemptions from the tax expressly designed to foster various local liquor industries. From 1960 to 1965, when the rate of tax was 16%, okolehao (a brandy distilled from the roots of the ti plant) produced in Hawaii was exempted from the tax.[2] This exemption expired in 1965, was reenacted in 1971,[3] was extended again in 1976,[4] and expired in 1981. The same 1976 enactment granted a five-year exemption to wine made in Hawaii from fruit grown in the State.[5] This exemption was allowed to lapse in 1981. While the present case was pending before the Hawaii Supreme Court, however, the legislature enacted and the governor approved a new exemption for "rum manufactured in the State for the period May 17, 1981 to June 30, 1986."[6]

The express intent of these exemptions is to promote the development and growth of local industry through discriminatory protection from the tax imposed on alcoholic beverages imported from foreign countries or the other 49 states. The stated purpose of the original 1960 exemption

and also includes, in addition to the foregoing, any spirituous, vinous, malt or fermented liquor, liquids, and compounds, whether medicated, proprietary, patented, or not, in whatever form and of whatever consistency and by whatever name called, containing one-half of one per cent or more of alcohol by volume, which are fit for use or may be used or readily converted for use for beverage purposes.

[2] 1960 Haw. Sess. Laws, c. 26, § 1.

[3] 1971 Haw. Sess. Laws, c. 62, § 1.

[4] 1976 Haw. Sess. Laws, c. 39, § 1 (H.R.S. § 244-4(6)).

[5] 1976 Haw. Sess. Laws, c. 39, § 1 (H.R.S. § 244-4(7)).

[6] 1981 Haw. Sess. Laws, c. 182, § 1 (H.R.S. § 244-4(8)).

for okolehao was "to encourage and promote the establishment of a new industry."[7] The 1976 exemptions were justified by the Senate Ways and Means Committee as follows:[8]

> The purpose of this bill is to extend the exemption of okolehao manufactured in the State from the liquor tax for an additional five years, to June 30, 1981. It is hoped that this five-year extension will aid the local okolehao industry to get on a firm financial foundation.
>
> Your Committee has amended this bill to provide a similar five-year exemption to the local fruit wine industry. Testimony received indicated that there may be an economic potential to the State in this area which, hopefully, this bill can help stimulate.

The Conference Committee Report on the latest exemption, for Hawaii-made rum, shows that the legislative purpose of favoring local industry continues:[9]

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[7] 1960 Haw. Sen. Journal, Standing Comm. Rep. No. 87. In its original form, the legislation exempted the sole manufacturer by name. *Ibid.; see* Standing Comm. Report No. 222.

[8] 1976 Haw. Sen. Journal, Standing Comm. Rep. No. 406-76.

[9] 1981 Haw. Sen. Journal, Conf. Comm. Rep. No. 29. The debate on the Report was as follows:

> Senator Abercrombie moved that Conf. Comm. Rep. No. 29 be adopted and H.B. No. 247, S.D. 2, C.D. 1, having been read throughout, pass Final Reading, seconded by Senator Henderson.
>
> Senator Kawasaki rose to speak against the measure as follows:
>
> "Mr. President, generally, I support giving tax exemption to new industries, particularly regarding the manufacture of Hawaiian Liquor, but I have some doubts about an arbitrary five-year exemption that we are providing this particular industry. I'd like to allow them the exemption as long as they need it but a blanket five years without showing cause for it might not be the wisest thing. For that reason, I'd like to vote against this bill."

The purpose of this bill is to exempt rum manufactured in the State from the liquor tax for five years. . . . Your Committee is aware of the consolidated cases in the State Tax Appeal court, Civil Nos. 1852, 1862, 1866 and 1867, under the name *Bacchus Imports, Ltd., et al. v. Freitas,* currently pending in the State Supreme Court, regarding the validity of certain liquor tax exemptions, and has had extensive discussions with the Attorney General's Office and the State Tax Department regarding the cases. Your Committee also notes that opinions conflict as to whether or not the national tax structure provides an advantage to rum produced in Puerto Rico and therefore makes no findings on that issue. Your Committee does feel, however, that providing a tax incentive in the form of a liquor tax exemption for a period of years is an appropriate method of encouraging the development of a new industry in the State and is therefore in agreement with the intent of the bill.

The discrimination created by the exemption is significant, reflecting both the rate of the tax and its incidence. An alcoholic beverage bottled at a cost of $10.00 will sell in Hawaii for $32.20 if it has been imported from France, but will sell for just $19.10 if bottled in Hawaii. Nearly half of this difference, or $6.50, is accounted for by the 20% tax. JA 11.

Senator Henderson remarked:

"Mr. President, we have consistently given five-year exemptions, in the initial periods, to these alcohol industries."

Senator Cayetano added his remarks as follows:

"Mr. President, voting with reservations for the bill, my concern is that with respect to new industries, it seems that we have taken a very selective approach. There's really no rationale for us to give one new industry tax exemption status over another. I suggest that when we come into session next year we consider a more comprehensive approach."

Id., 59th Day, at p. 751.

The rate of the tax can cause a similarly exaggerated price differential between two products originating outside of Hawaii. The size of the price differential, which ordinarily would be attributable solely to the freight charges involved, is exacerbated by the 20% surcharge. Thus the same bottle costing $10.00 to manufacture which sells for $32.20 if imported from France will sell for $23.80 if shipped from California. In this case, $2.20 (or more than 25%) of the differential represents the increase added by the Hawaii tax on the freight, shipping, and related markups attributable to the imported bottle. A substantial share of the revenues derived from the tax thus represents a surcharge on the transportation and importation costs for products imported from sister states and foreign countries. JA 11.

Appellant Bacchus made its May 1979 payment of liquor tax under protest,[10] and cited as grounds therefor that the Hawaii Liquor Tax violated the Import-Export and Commerce Clauses of the United States Constitution. JA 13. In June 1979 it filed suit on the same grounds in the Hawaii Tax Appeal Court, and appellant Eagle followed with its payment under protest in August 1979 and its complaint in September 1979. JA 13; 7. By subsequent stipulation, there was later added by amendment to each complaint a claim that the tax violated the Equal Protection Clauses of both the United States and Hawaii Constitutions. The cases were consolidated and heard on stipulated facts in the Hawaii Tax Appeal Court. The decision of that court, written by the Hawaii Attorney General's office on the ex parte request of the tax appeal court (see AJS at A-41), ruled on plaintiff's Import-Export Clause and Commerce Clause contentions, holding in favor of the tax, but did not deal with the Equal Protection arguments.

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[10]Payment of taxes under protest, and subsequent suit for their refund, are provided for in H.R.S. § 40-35, as amended.

The appeals to the Hawaii Supreme Court were consolidated, and briefed and argued on the facts stipulated in the tax appeal court. Again appellants raised the constitutional issues argued below. In an opinion that rejected each of appellants' contentions with respect to those issues, the Hawaii Supreme Court ruled that the tax was constitutional.

The highest state court based its conclusion on a misreading of this Court's consistent rulings prohibiting discriminatory state taxes. The Hawaii court's answer to appellants' claim of discrimination between Hawaiian and non-Hawaiian products was that the Hawaii tax treated Hawaiians and non-Hawaiians alike. Thus, the court's response to the patent discrimination of the statute was to deny discrimination because every wholesaler was subject to the same tax in the same manner. This analysis overlooked the clear command of more than a century of Commerce Clause jurisprudence. State laws that discriminate against out-of-state *products* are invalid, as are those that discriminate against out-of-state individuals.

SUMMARY OF ARGUMENT

The Hawaii Liquor Tax at issue in this case discriminates on its face against alcoholic beverages imported from sister states and foreign countries. That discrimination renders the tax unconstitutional *per se*.

Protectionist statutes and statutes that discriminate on their face against interstate commerce are invalid *per se* under the Commerce Clause. *Maryland v. Louisiana,* 451 U.S. 725 (1981); *Boston Stock Exchange v. State Tax Commission,* 429 U.S. 318 (1977). The record in this case shows that the Hawaii Liquor Tax was designed for the express purpose of fostering local industry at the expense of interstate and foreign commerce. Hawaii's protectionist purpose, and the discriminatory language of the statute itself, make further inquiry into the operation or effect of the tax unnecessary.

The Hawaii tax, by discriminating against alcoholic beverages imported from abroad as well as against those shipped from other states, violates the foreign Commerce Clause. *Cook v. Pennsylvania*, 97 U.S. 566 (1878). The discriminatory tax on imported products is, in addition, a state-imposed duty on imported liquor which violates the Import-Export Clause. *Michelin Tire Corp. v. Wages*, 423 U.S. 276, 288 n.7 (1976); *Department of Revenue v. James B. Beam Distilling Co.*, 377 U.S. 341 (1964). The protectionist discrimination between Hawaiian and non-Hawaiian alcoholic beverages also violates the Equal Protection Clause because it creates a classification which is not sustained by any legitimately rational basis. *Compare Wheeling Steel Corp. v. Glander*, 337 U.S. 562 (1949) *with Allied Stores of Ohio, Inc. v. Bowers*, 358 U.S. 522 (1959). *Cf. Southern Ry. Corp. v. Greene*, 216 U.S. 400 (1910).

Section 2 of the Twenty-first Amendment does not justify the liquor tax. Neither the history nor the language of the amendment provides any support for a discriminatory tax of the type involved in this case. *See California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97 (1980); *Craig v. Boren*, 429 U.S. 190 (1976); *Hostetter v. Idlewild Bon Voyage Liquor Corp.*, 377 U.S. 324 (1964). The protectionist purpose of the Hawaii Liquor Tax cannot prevail over the dominant federal interest in free trade.

ARGUMENT

I

THE DISCRIMINATORY HAWAII LIQUOR TAX VIOLATES THE COMMERCE CLAUSE

The Hawaii Liquor Tax is, by design, a protectionist measure. It seeks to foster local industry at the expense of foreign and interstate commerce. On its face it discriminates against products solely because of their out-of-state origin. It thus violates what this Court has held, in *Boston Stock Exchange v. State Tax Commission*, 429 U.S.

318 (1977), to be a "fundamental principle" of Commerce Clause jurisprudence:

> No State, consistent with the Commerce Clause, may "impose a tax which discriminates against interstate commerce . . . by providing a direct commercial advantage to local business."

429 U.S. at 329 (citation omitted).

A. The Basic Purpose of the Commerce Clause Is to Prevent Isolationist and Protectionist Measures like the Hawaii Liquor Tax

The failure of the Articles of Confederation to prohibit the individual states from advancing their own commercial interests by discriminating against goods from other states was "a compelling reason for the calling of the Constitutional Convention of 1787. . . ." *Michelin Tire Corp. v. Wages*, 423 U.S. 276, 283 (1976). Economic warfare among the states convinced the Framers that "in order to succeed, the new Union would have to avoid the tendencies toward economic Balkanization that had plagued relations among the colonies and later among the States under the Articles of Confederation." *Hughes v. Oklahoma*, 441 U.S. 322, 325-26 (1979).

The Commerce Clause was the solution. It grants to Congress the power "[t]o regulate Commerce with foreign Nations, and among the several States . . . ." U.S. Const. art. I, § 8, cl. 3. As this Court has long recognized, the Commerce Clause does more than enable Congress to enact legislation. It also prohibits a state from erecting barriers against the free flow of interstate and foreign trade even in the absence of congressional action. *Freeman v. Hewit*, 329 U.S. 249, 252 (1946). That prohibition is basic to the federal system established by the Constitution:

> This principle that our economic unit is the Nation, which alone has the gamut of powers necessary to control the economy, including the vital power of erecting customs barriers against foreign competition, has as

its corollary that the states are not separable economic units. As the Court said in *Baldwin v. Seelig*, 294 U.S. 511, 527, "What is ultimate is the principle that one state in its dealings with another may not place itself in a position of economic isolation. . . ."

. . . .

Our system, fostered by the Commerce Clause, is that every farmer and every craftsman shall be encouraged to produce by the certainty that he will have free access to every market in the Nation, that no home embargoes will withhold his export, and no foreign state will by customs duties or regulations exclude them. Likewise, every consumer may look to the free competition from every producing area in the Nation to protect him from exploitation by any. Such was the vision of the Founders; such has been the doctrine of this Court which has given it reality.

H.P. Hood & Sons, Inc. v. Du Mond, 336 U.S. 525, 537-39 (1949). In consistently striking down laws by which states have attempted to isolate their economies and protect their local businesses from interstate competition, this Court has focused on the incompatibility of such protectionist measures with the basic purpose of the Commerce Clause "to create an area of free trade among the several States"[11] which would remain "free from interference by the States."[12]

B. Protectionist Laws and Laws that Discriminate on Their Face Are Unconstitutional Per Se

Although the Court has recognized that an incidental burden on interstate commerce may be permitted when a state acts to further a legitimate local public interest, "where simple economic protectionism is effected by state legislation, a virtually *per se* rule of invalidity has been erected." *Philadelphia v. New Jersey,* 437 U.S. 617, 624

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[11]*McLeod v. J.E. Dilworth Co.,* 322 U.S. 327, 330 (1944).

[12]*Freeman v. Hewit,* 329 U.S. 249, 252 (1946).

(1978).[13] Despite the Court's description of the rule as one of "virtually" *per se* invalidity, it is clear that economic protectionism "is *impermissible* under the Commerce Clause." *Kassel v. Consolidated Freightways Corp.*, 450 U.S. 662, 685 (1981) (Brennan, J., concurring). The cases demonstrate that a finding of protectionism is fatal to a statute discriminating against interstate commerce.

In addition, *any* statute that discriminates on its face against interstate commerce is, even in the absence of evidence of the state's purpose, so suspect under the Commerce Clause that the burden is cast upon the state to prove its constitutionality. *Hughes v. Oklahoma*, 441 U.S. 322, 336 (1979). As this Court held in *Hughes*:

> [F]acial discrimination [against interstate commerce] by itself may be a fatal defect, regardless of the state's purpose, because "the evil of protectionism can reside in legislative means as well as legislative ends." At a minimum such facial discrimination involves the strictest scrutiny of any purported legitimate local purpose and the absence of nondiscriminatory alternatives.

441 U.S. at 337 (citation omitted).[14] Thus, a discriminatory statute is invalid unless the state shows that there is no

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[13] *See also Lewis v. BT Investment Managers, Inc.*, 447 U.S. 27, 36 (1980) (citation omitted):

> Over the years, the Court has used a variety of formulations for the Commerce Clause limitation upon the States, but it consistently has distinguished between outright protectionism and more indirect burdens on the free flow of trade. The Court has observed that "where simple economic protectionism is effected by state legislation, a virtually *per se* rule of invalidity has been erected."

[14] *See also Minnesota v. Clover Leaf Creamery Corp.*, 449 U.S. 456, 471 n.15 (1981) (discriminatory effect can invoke *per se* rule); *Philadelphia v. New Jersey*, 437 U.S. 617, 626-27 (1978):

> [w]hatever [the state's] ultimate purpose, it may not be accomplished by discriminating against articles of commerce coming from outside the State unless there is some reason, apart from their origin, to treat them differently.

nondiscriminatory method of achieving any legitimate purpose it is alleged to serve.

C. The Hawaii Liquor Tax Is Unconstitutional Per Se

This case presents the Court with an avowedly protectionist statute that discriminates on its face against interstate commerce for no legitimate reason. It is unconstitutional both for its protectionist purpose and for its unjustifiable discrimination.

1. The Per Se Rule Applies Because of Hawaii's Impermissible Protectionist Objective

The protectionist purpose of Hawaii's Liquor Tax is beyond question. According to the Hawaii Legislature, the exemptions from tax for locally produced okolehao, wine, and rum were meant "to encourage and promote the establishment of a new industry," to "aid the local okolehao industry," and to stimulate "economic potential to the state in this area [of local wine production]."[15] The state has never disavowed these protectionist purposes. To the contrary, protectionism is the *only* purpose Hawaii advances to justify the discrimination. The state argues that the tax savings realized by Hawaii okolehao producers "could be channelled into a national promotion campaign and competitive pricing," that jobs would be generated by favoring Hawaii producers, that the "benefit to the industry and ultimately the State of Hawaii" justified the discrimination, and that the tax scheme "would give [the wine industry] a stimulus to become a solid, financially sound industry."[16]

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[15]See Statement of the Case, *supra*. The legislature has consistently expressed a protectionist purpose in enacting the various exemptions.

[16]Record ("R.") 268. With such a clear articulation of protectionism as the sole purpose of the Hawaii Liquor Tax, no hypothetical legislative objectives should be considered. *Minnesota v. Clover Leaf Creamery Corp.*, 449 U.S. at 471 n.15; J. Eule, *Laying the Dormant Commerce Clause To Rest*, 91 Yale L. J. 425, 457 (1982).

Thus, the Hawaii Liquor Tax is, by its nature and purpose, a protectionist assault on the basic free trade purpose of the Commerce Clause. If it were allowed to stand it "'would invite a multiplication of preferential trade areas destructive' of the free trade which the Clause protects." *Boston Stock Exchange v. State Tax Commission*, 429 U.S. 318, 329 (1977) (quoting *Dean Milk Co. v. Madison*, 340 U.S. 349, 356 (1951)). A statute enacted for such plainly protectionist reasons cannot survive Commerce Clause scrutiny.

Boston Stock Exchange provides an example of the Court's application of the *per se* rule to a tax designed to foster local industry. Concerned by the growth of securities exchanges in other states, New York enacted a transfer tax on sales of securities that discriminated on its face against sales in other states.[17] The transfer tax's express purpose was to provide a commercial advantage to the New York Stock Exchange and other in-state exchanges. The legislature, the governor, and the New York Stock Exchange (as the law's primary intended beneficiary), all acknowledged that the state's objective was to promote New York's exchanges at the expense of those in other states. 429 U.S. at 323-28. The statute's protectionist nature thus was unquestioned, and no further showing as to its discriminatory effect was necessary. The Court unanimously held that the statute violated the "fundamental

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In any event, the state has not attempted to justify the tax as furthering any other objectives, and the Hawaii Supreme Court accepted the legislative history as an accurate statement of the tax's purpose. AJS A-12 to A-13.

[17]For nonresidents of New York the tax on in-state securities sales was only one-half of the tax on out-of-state sales. In addition, instate sales by either nonresidents or residents were subject to a maximum tax of $350, while out-of-state sales were taxed without limitation, based solely on the size of the transaction.

principle" that no state could, through its tax scheme, favor local business over interstate commerce. 429 U.S. at 329.[18]

An earlier New York statute, also enacted for protectionist purposes, was held unconstitutional in ***Baldwin v. G.A.F. Seelig, Inc.***, 294 U.S. 511 (1935). A provision of the New York Milk Control Act setting minimum prices to be paid by dealers to New York milk producers had previously been upheld by the Court in ***Hegeman Farms Corp. v. Baldwin***, 293 U.S. 163 (1934). In ***Seelig***, however, the Court was faced with a challenge to another provision of the Act that discriminated against interstate commerce. The provision challenged in ***Seelig***, in order "[t]o keep the system unimpaired by competitors from afar," 294 U.S. at 519, barred the sale of milk from other states if the out-of-state producer was paid less than the New York minimum price. New York acknowledged that its purpose was to protect New York milk producers by eliminating the competitive advantage of other producers. *Id.* at 522, 523, 527. The Court struck the law down, holding that when "the avowed purpose of the obstruction, as well as its necessary tendency, is to suppress or mitigate the consequences of competition between the states . . . [then] by the very terms of the hypothesis" the statute imposes an unconstitutional burden on interstate commerce. *Id.* at 522. ***See also Kassel v. Consolidated Freightways Corp.***, 450 U.S. 662, 682 n.3, 685-87 (1981) (Brennan, J., concurring) (Court should not reach question of law's practical burden on interstate commerce because state's protectionist purpose requires Court to hold law invalid ***per se***).

The Hawaii Liquor Tax, like the laws struck down in ***Boston Stock Exchange*** and ***Seelig***, is protectionist. It, too, is unconstitutional.

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[18] The Court rejected, without going beyond the statute's face, the state's arguments that the statute was (1) nondiscriminatory in its practical effect and (2) a valid "compensatory" tax under ***Henneford v. Silas Mason Co.***, 300 U.S. 577 (1937).

2. The Hawaii Liquor Tax Is Invalid Because Its Facial Discrimination Against Interstate Commerce Is Unjustifiable

Even if no protectionist purpose is found, a discriminatory state tax is invalid unless the state comes forward with a legitimate local objective and a showing that it had no less discriminatory means to attain that objective. *Hughes v. Oklahoma*, 441 U.S. at 337.

On numerous occasions the Court has struck down facially discriminatory taxes for which no legitimate purpose or need was shown. In *Maryland v. Louisiana*, 451 U.S. 725 (1981), the Court reviewed a Louisiana tax on natural gas that on its face imposed a greater burden on interstate commerce than on intrastate commerce. The tax's facial discrimination was enough to justify application of the *per se* rule because the state's purported justifications did not satisfy the "strictest scrutiny" the Court gives to discriminatory statutes.

The Court used the same analysis to strike down a Tennessee law substantially identical to the Hawaii Liquor Tax in *I. M. Darnell & Son Co. v. Memphis*, 208 U.S. 113 (1908). The Tennessee tax's discrimination against interstate commerce was clear. It taxed all property in the state other than "the direct product of the soil of this state in the hands of the producer and his immediate vendee, and manufactured articles from the produce of the state in the hands of the manufacturer." 208 U.S. at 115.

The Tennessee tax had many of the characteristics that the Hawaii Supreme Court thought established the constitutional validity of the Hawaii tax. Tennessee imposed a tax on *all* goods and then granted exemptions to in-state products. Tennessee treated all taxpayers equally, whether state residents or not; the tax discriminated only against *goods* from other states. As is the case with the Hawaii Liquor Tax, the "burden" of the Tennessee tax could be said to fall wholly within the state. Finally, Darnell could

have reduced its tax burden simply by dealing exclusively in Tennessee products.[19]

However, Tennessee failed to show any legitimate purpose for the discrimination. The tax's constitutionality was therefore "clearly foreclosed by prior decisions of this court." 208 U.S. at 119. Those decisions had "long since clearly established the want of power in a state to discriminate by taxation in any form against property brought from other states." *Id.* at 120-21. *See also Hughes v. Oklahoma,* 441 U.S. 322 (1979) (state law discriminating on its face against interstate commerce in minnows held invalid *per se*); *Welton v. Missouri,* 91 U.S. 275 (1876) (Missouri tax on peddlers selling goods manufactured outside Missouri held to discriminate against interstate commerce in an unconstitutional manner).[20]

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[19]The Hawaii Supreme Court apparently believed the ability of a taxpayer to avoid the liquor tax by switching to Hawaiian wine was a point in favor of its constitutionality. AJS A-25. But a state tax which is designed to, and does, create incentives to shift economic activity into the state is for that very reason unconstitutional. *Boston Stock Exchange v. State Tax Commission,* 429 U.S. 318, 331, 335-36 (1977).

[20]In *Guy v. Baltimore,* 100 U.S. 434, 439, 442 (1880) the Court stated the same rule:

> In view of these and other decisions of this court, it must be regarded as settled that no State can, consistently with the Federal Constitution, impose upon the products of other States, brought therein for sale or use, . . . more onerous public burdens or taxes than it imposes upon the like products of its own territory.
>
> . . . .
>
> . . . The concession of such a power to the States would render wholly nugatory all national control of commerce among the States, and place the trade and business of the country at the mercy of local regulations, having for their object to secure exclusive benefits to the citizens and products of particular States.

Guy held unconstitutional duties imposed by Baltimore solely on goods "other than the product of the State of Maryland."

The vice of the taxes in the above cases was that they, like the Hawaii Liquor Tax, were crafted to promote local interests. But even a statute that does not directly benefit local business is invalid if it discriminates on its face against interstate commerce. In *Philadelphia v. New Jersey*, 437 U.S. 617, 624 (1978), New Jersey landfill operators were among those challenging New Jersey's ban on the transportation of waste products into the state for disposal. 437 U.S. at 626. The Court assumed that the law conferred no benefit on local business and that the purpose of the statute was, as expressed by the state legislature, to protect the environment and the public health and safety. But the law's discriminatory *means* were just as objectionable as a protectionist purpose. New Jersey failed to show any reason—apart from origin—why it needed to discriminate against waste products from other states. Moreover, an evenhanded law treating all waste equally was a feasible and less discriminatory alternative.

An unjustified discriminatory tax on any product, including alcoholic beverages, *e.g.*, *Walling v. Michigan*, 116 U.S. 446 (1886), is unconstitutional. Hawaii has identified no legitimate objective served by its tax. Accordingly, the tax's facial discrimination requires that it be held invalid.

D. The State's Arguments That the Hawaii Liquor Tax Does Not Discriminate Against Interstate Commerce Are both Irrelevant and Incorrect

Despite the protectionist nature of the liquor tax and its violation of the fundamental Commerce Clause principle prohibiting taxes that discriminate against interstate commerce, the state nonetheless attempts to assert the tax's constitutionality. Hawaii's claim is that the tax does not discriminate. But the nondiscrimination arguments advanced by the attorney general—and adopted seemingly without question by the Hawaii Supreme Court—are without any basis.

Although not clearly elaborated by the state or by the Hawaii court's opinion, the nondiscrimination argument ap-

pears to be based upon two propositions: (1) that appellants did not make a sufficient showing of the liquor tax's practical discriminatory operation; and (2) that, in any event, the liquor tax does not discriminate against interstate commerce because all taxpayers, whether Hawaiian or not, are treated equally. Neither proposition supports the conclusion the state desires.[21]

1. Given Hawaii's Protectionist Purpose and the Liquor Tax's Facial Discrimination, Appellants Were Not Required to Show Discrimination in the Tax's Practical Operation

The Hawaii Supreme Court ignored the rule that a state law with protectionist purposes, or one that is discriminatory on its face, is invalid *per se*. Instead, the court held that "taxpayers have failed to demonstrate that the Hawaii Liquor Tax in its *practical operation* works discrimination against interstate commerce." AJS A-50 (emphasis added). Both the imposition of this burden and the conclusion that it was not sustained were erroneous.

First, when a tax is protectionist, as in this case, there is neither a reason nor a need to consider its practical operation. *Baldwin v. G.A.F. Seelig*, 294 U.S. at 522 (direct or indirect burdens on commerce "are irrelevant when the avowed purpose of the obstruction . . . is to suppress or mitigate the consequences of competition between the

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[21]The state has also claimed that because some Hawaiian liquor (sake and fruit liquors) is taxed, there is no discrimination against interstate commerce. R. 269, 276-78. The Hawaii Supreme Court apparently found this argument to have some force. AJS A-21 n.15.

This argument proves far too much. It would allow a state to justify almost any tax discriminating against interstate commerce merely by subjecting *some* local products to the tax, reducing the Commerce Clause to empty words. Of course, such superficial analysis has not prevailed. *See, e.g., Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64 (1963) (Louisiana tax discriminating against interstate commerce only in the context of certain unique, isolated transactions, and apparently only because of an accident of statutory drafting, nonetheless held unconstitutional).

states"). Similarly, evidence of the practical operation of a statute discriminating on its face against interstate commerce is irrelevant. Only where (1) legitimate state objectives are credibly advanced, (2) there is no patent discrimination against interstate trade, and (3) the effect on interstate commerce is incidental, will the Court look past legislative history and facial discrimination to consider the law's practical effect and relative burden on commerce.[22] *Philadelphia v. New Jersey,* 437 U.S. 617, 624 (1978); *Pike v. Bruce Church, Inc.,* 397 U.S. 137, 142 (1970).

Second, the Hawaii tax inexorably discriminates against interstate commerce by its very terms, and no further evidence was necessary. Any burden of showing discrimination was met conclusively by the terms of the statute. *See Allied Stores of Ohio, Inc. v. Bowers,* 358 U.S. 522, 529-30 (1959).

2. A Tax That Discriminates Against Products in Interstate Commerce Is Unconstitutional Even if In-State and Out-of-State Taxpayers Are Treated Equally

The Hawaii Supreme Court, ignoring the disparate treatment of liquor products according to place of origin, focused on the equal treatment purportedly received by all *taxpayers*:

> Bacchus, Paradise, and Eagle gain nothing over a foreign corporation because of their incorporation under Hawaii law. That McKesson is a Maryland corporation and engaged in business elsewhere plays no part in fixing its liability under HRS § 244-4. The corporation presumably is also free to engage in the wholesaling of

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[22]The best example from this Court's decisions is the "compensating" tax approved in *Henneford v. Silas Mason Co.,* 300 U.S. 577 (1937). Because both the objective and the "practical operation" of Washington's compensatory use tax was to *equalize* the burden on interstate and intrastate commerce, it was held valid under the Commerce Clause. No similar argument is available to Hawaii.

okolehao and pineapple wine if it has reason to believe this will relieve its tax burden.

The Hawaii court tried to distinguish *Maryland v. Louisiana*, 451 U.S. 725 (1981), *Boston Stock Exchange v. State Tax Commission*, 429 U.S. 318 (1977), and *Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64 (1963) as cases in which the burden of the discrimination fell out-of-state. AJS A-25 to A-29.[23]

But this case involves a claim of discrimination against out-of-state *products*. The Commerce Clause protects goods in interstate commerce regardless of the residence of those on whom the burden of the state's discrimination falls. *Philadelphia v. New Jersey*, 437 U.S. at 626-27 ("whatever New Jersey's purpose, it may not be accomplished by discriminating against articles of commerce coming from outside the state"); *I.M. Darnell & Son Co. v. Memphis*, 208 U.S. 113 (1908) (Tennessee tax discriminating against products from other states held unconstitutional).

The Hawaii Liquor Tax's unlawful protectionist purpose and discriminatory burden on commerce are not mitigated by the fact that both Hawaiian and non-Hawaiian taxpayers must pay its unconstitutional levy. *Minnesota v. Barber*, 136 U.S. 313, 326 (1890).

II

THE IMPOSITION OF THE HAWAII LIQUOR TAX ON IMPORTS VIOLATES THE FOREIGN COMMERCE CLAUSE AND THE IMPORT-EXPORT CLAUSE

In addition to bringing wine into Hawaii from other states, Bacchus and Eagle import wine from foreign countries. JA 9, 14. The Hawaii Liquor Tax, by taxing the first

[23]The Hawaii Supreme Court was surprised a Hawaii resident would even complain:

> We noted earlier that Paradise, a Hawaii corporation engaged in the wholesaling of okolehao, also claims the tax violates the Commerce Clause. . . .
>
> We find it difficult to give much credence to a claim that the tax creates an undue burden on interstate commerce when the

sale of imports by Bacchus and Eagle while exempting Hawaiian products, violates both the foreign Commerce Clause and the Import-Export Clause.

A. By Discriminating Against Imports the Hawaii Liquor Tax Violates the Foreign Commerce Clause

The Commerce Clause applies not only to interstate commerce but also to "Commerce with foreign Nations." U.S. Const. art. I, § 8, cl. 3. The Court's interpretation of the foreign Commerce Clause has, for the most part, paralleled its analysis of the interstate Commerce Clause, *see* section I.C., *supra*, although the Court has recently stated that the states' power to regulate foreign commerce is even more limited because "the taxation of foreign commerce may necessitate a uniform national rule." *Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. 434, 449 (1979).[24] As a result of the need for national uniformity, the fundamental principle of nondiscrimination recognized in the area of interstate commerce applies with equal if not greater force under the foreign Commerce Clause. *Cook v. Pennsylvania*, 97 U.S. 566 (1878).

Two Pennsylvania taxes were challenged in *Cook*. The first statute imposed a tax of one-half of one percent on the sale price of "all domestic articles and groceries" sold at auction while taxing "foreign drugs, glass, earthenware, hides, marble-work, and dye-woods" sold at auction at the rate of three-quarters of one percent. The second statute amended the first to impose a tax on auctioneers of one-quarter of one percent on all sales of "loans or stocks"

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argument is advanced by one who logically would be a "beneficiary" of the alleged discrimination.

AJS A-38 n.17.

[24]"Although the Constitution . . . grants Congress power to regulate Commerce 'with foreign Nations' and 'among the several States' in parallel phrases, there is evidence that the Founders intended the scope of the foreign commerce power to be the greater." *Japan Line, Ltd.*, 441 U.S. at 448.

and "on all other sales as aforesaid, except on groceries, goods, wares, and merchandise of American growth or manufacture." 97 U.S. at 569. The Court held both taxes invalid under the foreign Commerce Clause:

> In *Woodruff v. Parham* (8 Wall. 123) and *Hinson v. Lott* (id. 148) it was held that a tax laid by a law of the State in such manner as to discriminate unfavorably against goods which were the product or manufacture of another State, was a regulation of commerce between the States, forbidden by the Constitution of the United States. . . . The Congress of the United States is granted the power to regulate commerce with foreign nations in precisely the same language as it is that among the States. If a tax assessed by a State injuriously discriminating against the products of a State of the Union is forbidden by the Constitution, a similar tax against goods imported from a foreign State is equally forbidden.

97 U.S. at 573.[25] *See also Welton v. Missouri*, 91 U.S. 275 (1876) (tax discriminating against goods from foreign countries and other states violates interstate and foreign components of Commerce Clause); *Brown v. Maryland*, 25 U.S. (12 Wheat.) 419, 448 (1827) (discriminatory tax on imports held invalid under foreign Commerce Clause and Import-Export Clause).

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[25]In reaching this holding the Court rejected several arguments on which Hawaii now relies, over one hundred years later. For example, the state has argued that Hawaii's liquor tax is not on the imported goods but on the privilege of doing business. R. 264. Precisely that argument was rejected in *Cook*. 97 U.S. at 570-73. Another argument made below and accepted by the Hawaii court—that the liquor tax is not discriminatory because it treats all taxpayers alike—was also unsuccessful in *Cook*. 97 U.S. at 573 (focus is on discrimination against *goods*). Finally, Hawaii has contended that, because its liquor tax superficially taxes *all* liquor and exempts only *some* Hawaiian liquor from tax, it does not discriminate in favor of local products. R. 269. But *Cook* invalidated precisely such a scheme.

The Hawaii Liquor Tax, like the tax struck down in *Cook*, discriminates on its face against liquor imported by Bacchus and Eagle by taxing such imports while exempting Hawaiian products. Hawaii thus treats foreign imports differently from its local goods. This discrimination is no more valid than the discrimination against products of sister states.

B. By Taxing Imports on the Basis of Their Origin the Hawaii Liquor Tax Violates the Import-Export Clause

The Constitution provides that "[n]o State shall . . . lay any Imposts or Duties on Imports or Exports." U.S. Const. art. I, § 10, cl. 2. "[T]he Import-Export Clause states an absolute ban" on the states' power to tax. *Department of Revenue v. Ass'n of Washington Stevedoring Cos.*, 435 U.S. 734, 751 (1978). As shown below, the Hawaii Liquor Tax is a duty on imports and therefore violates the clause's absolute ban.

1. Taxes Imposed on Imports Because of Their Foreign Origin Fall Within the Absolute Ban of the Import-Export Clause

In *Department of Revenue v. James B. Beam Distilling Co.*, 377 U.S. 341 (1964), the Court was presented with a challenge to a Kentucky statute prohibiting importation of distilled spirits without payment of a tax of ten cents per proof gallon.[26] The tax was thus imposed on imports solely because of their origin. Beam objected to the imposition of this tax on whisky imported from Scotland, contending

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[26] The Kentucky law provided:

> No person shall ship or transport or cause to be shipped or transported into the state any distilled spirits from points without the state without first obtaining a permit from the department and paying a tax of ten cents on each proof gallon contained in the shipment.

377 U.S. at 342. The Kentucky tax, like the Hawaii Liquor Tax, applied to both interstate and foreign alcoholic beverages.

that it was unconstitutional under the Import-Export Clause as an impost or duty on imports. The Court agreed that the tax was "clearly of a kind prohibited by the Export-Import Clause," 377 U.S. at 343, and ruled it unconstitutional.

Beam broke no new ground in holding unconstitutional a state tax discriminating against imports on the basis of their foreign origin. Indeed, *Cook v. Pennsylvania* reached a similar conclusion. In *Cook*, as already noted, two Pennsylvania tax statutes discriminated against imports, in one instance by taxing domestic articles at a lower rate, and in the other by imposing the tax on all imports while exempting certain domestic articles (but like Hawaii, not all). After rejecting Pennsylvania's argument that the tax was on the privilege of auctioning goods rather than on the imports themselves, the Court held the discriminatory tax void as "laying a duty on imports." 97 U.S. at 573. *See also People v. Maring*, 3 Keyes 374 (N.Y. Ct. App. 1867) (tax discriminating against the sale of "foreign wines and ardent spirits" and other imports held to violate Import-Export Clause).[27]

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[27]In *Welton v. Missouri*, 91 U.S. 275 (1876), the Court struck down a tax imposed on peddlers of goods other than those which were the growth, product, or manufacture of Missouri. Although the tax was invalidated under the Commerce Clause, the Court borrowed heavily from Import-Export Clause jurisprudence, including the seminal case of *Brown v. Maryland*, 25 U.S. (12 Wheat.) 419 (1827). In holding that Missouri had invaded a province of exclusive federal power, the Court emphasized that it was the tax's discrimination on the basis of foreign origin which condemned it, and noted that under either the Commerce or Import-Export Clauses

> [t]he commercial power [of Congress] continues until the commodity has ceased to be the subject of discriminating legislation by reason of its foreign character. That power protects it, even after it has entered the State, from any burdens imposed by reason of its foreign origin.

91 U.S. at 282. As discussed below, *Welton* and *Cook* presaged the Court's analysis in *Michelin Tire Corp. v. Wages*, 423 U.S. 276 (1976).

2. The Court's Michelin Decision Provides Recent Authority for the Continuing Validity of Beam and Cook and for the Conclusion That the Hawaii Liquor Tax Is Unconstitutional

In *Michelin Tire Corp. v. Wages*, 423 U.S. 276 (1976), the Court was faced with an Import-Export Clause challenge to a Georgia ad valorem property tax. Michelin imported tires and stored them in a warehouse in Georgia for distribution in six southeastern states. Georgia assessed its nondiscriminatory ad valorem property tax on the value of Michelin's property in the state, including the imported tires. Michelin argued that the imported tires had not lost their character as imports and that, under *Low v. Austin*, 80 U.S. (13 Wall.) 29 (1872), Georgia's ad valorem property tax was unconstitutional as applied to the imported tires.[18]

The Court declined to decide whether the tires retained their character as imports. Instead, it reexamined what it found to be the three concerns of the Import-Export Clause: (1) that the federal government speak with one voice in regulating foreign commerce, without interference from State tariffs; (2) that federal revenues from import taxes not be diverted to the States; and (3) that there be no disharmony among the states caused by one state's imposing duties on imports destined for another state. These concerns would be frustrated, the Court held, by a discriminatory tax falling "on imports as such because of their place of origin." 423 U.S. at 286. Thus, "[t]he Import-Export Clause clearly prohibits state taxation based on the foreign origin of the imported goods." *Id.* at 287. Because Georgia's nondiscriminatory ad valorem property tax did not fall on

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[18] *Low* held that, as long as goods retained their character as imports, "a tax upon them, in any shape, is within the constitutional prohibition." 80 U.S. (13 Wall.) at 34. Accordingly, it invalidated a nondiscriminatory ad valorem property tax imposed by California on all property in the state including imported goods.

imports because of their origin, it did not implicate the Import-Export Clause's concerns and it was, therefore, constitutional. To the extent *Low* held otherwise it was overruled.

Michelin is fully consistent with *Beam* and *Cook*. Both of those cases, unlike *Low*, involved *discriminatory* taxes targeted at imports on the basis of their origin, precisely the sort of tax that *Michelin* reaffirmed is within the prohibition of the Import-Export Clause. 423 U.S. at 288 n.7. Neither case depends on the rejected original package doctrine of *Low*, and the Court itself has noted their continuing validity. *Michelin*, 423 U.S. at 288 n.7 (*Cook*); *California Retail Liquor Dealer Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 108 (1980) (*Beam*).

3. The Hawaii Liquor Tax Is an Unconstitutional Tax on Imports Under Beam, Cook, and Michelin

The Hawaii Liquor Tax, like the taxes struck down in *Beam* and *Cook*, is imposed on imports on the basis of their foreign origin. Hawaiian wine, brandy, and rum are not taxed; imported wine, brandy, and rum are. As *Michelin* makes clear, such discrimination, whether practiced at the moment of importation, at the time of wholesale, or at the point of retail sale, is by its very nature a duty on imports. 423 U.S. at 288 n.7.[29]

The Hawaii Supreme Court simply glossed over the fact that the liquor tax is imposed on products based on their foreign origin. Instead it upheld the tax because of its conclusion that "the Hawaii Liquor Tax offends none of the policy considerations delineated by the Court in *Michelin* . . ." AJS A-20 to A-21. This statement is demonstrably incorrect.

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[29]*Michelin* thus adopts the reasoning, originally stated in *Welton v. Missouri*, see note 27, *supra*, that the Import-Export Clause applies whenever a state attempts to discriminate against a product because of its foreign character.

The first policy consideration under the Import-Export Clause—that a state tax on imports would undermine the federal government's exclusive regulation of foreign commerce—is "the most important purpose of the Clause's prohibition." *Michelin*, 423 U.S. at 286. A state could use a tax on imports "to create special protective tariffs or particular preferences for certain domestic goods" or to "encourage and discourage . . . importation in a manner inconsistent with federal regulation." *Ibid.* The Hawaii Supreme Court's holding that the liquor tax presented none of these dangers ignores the plain fact that the very purpose of the Hawaii Legislature was to protect and nurture certain domestic industries. By its very nature the tax thus acts in derogation of the federal government's exclusive power to tax imports and regulate foreign commerce.

The Hawaii Liquor Tax also interferes with the federal government's exclusive right to duties on imports, the second policy concern of the Import-Export Clause, by substantially raising the price of imported wine, brandy, and rum relative to competing Hawaiian products. *See* Statement of Case, *supra.*[30] A principal fault of such a state tax is that it can be "selectively imposed and increased so as to substantially impair or prohibit importation," *Michelin*, 423 U.S. at 288, thereby affecting the import duties received by the federal government.

Thus Hawaii's tax is imposed on imports solely because of their foreign origin; it thereby invokes the two most important policy concerns inherent in the constitutional prohibition of state taxes on imports. Under any reason-

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[30]This is not a case, like *Department of Revenue v. Ass'n of Washington Stevedoring Cos.*, 435 U.S. 734, 753 (1978), where such effects can be considered "insubstantial." The *Stevedoring* case involved a mere 1% tax on the gross income of a stevedore's entire business. In contrast, Hawaii imposes a 20% tax on the wholesale price of the product itself, which can substantially raise its price. JA 11.

able reading of the Import-Export Clause the Hawaii tax is unconstitutional.[31]

III

SECTION 2 OF THE TWENTY-FIRST AMENDMENT DOES NOT SAVE THE DISCRIMINATORY TAX

Because this case involves a discriminatory state tax on alcoholic beverages, rather than other articles of commerce, it presents a potential issue as to whether the tax may be justified by section 2 of the Twenty-first Amendment. Section 2—on which the state has placed no reliance and which was not discussed by the courts below—provides no basis for discriminatory state taxes. Section 2 does not authorize protectionist state legislation nor concern any local interest involved in this case. The central purpose of section 2 was to allow states wishing entirely to exclude alcoholic beverages from their borders to do so. That purpose, and the history behind section 2, provide no more justification

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[31]The Hawaii court also rejected appellant's equal protection claims on the ground that the statute did not "establish a classificatory scheme that disfavors any of the taxpayers." AJS A-8. However, within a given class of taxpayers (such as liquor wholesalers), equal protection requires that all who are subject to a given law "shall be treated alike, under like circumstances and [conditions] both in the privileges conferred, and in the liabilities imposed." *Connolly v. Union Sewer Pipe Co.*, 184 U.S. 540, 559 (1902), quoting *Hayes v. Missouri*, 120 U.S. 68, 71 (1887). The taxation of appellants' goods of wine originating outside Hawaii, while exempting for illegitimate purposes the sales of Hawaiian products by taxpayers in competition with appellants, treats taxpayers in the same class differently in respect to the same transaction. *Compare Wheeling Steel Corp. v. Glander*, 337 U.S. 562 (1949) *with Allied Stores of Ohio, Inc. v. Bowers*, 358 U.S. 522 (1959). *Cf. Southern Ry. Corp. v. Greene*, 216 U.S. 400 (1910) (additional tax imposed on out-of-state corporation unconstitutional). *See State v. Bengsch*, 170 Mo. 81, 109, 113-117, 70 S.W. 710, 718-720 (1902) (gallonage tax imposed on all liquor manufactured or imported for sale in state, which exempted native wines, as well as liquor manufactured in state for export, violated equal protection clause).

for the promotion of a state's local alcoholic beverage industry through discriminatory taxation than does the language of section 2.

A. The Purpose of Section 2 of the Twenty-first Amendment Was to Provide a Constitutional Basis for Dry States to Remain Dry

Section 2 is limited by its terms to a prohibition on the "transportation or importation into any State" of alcoholic beverages in violation of state law. This narrow language reflects the history that led to section 2, and the limited state interests to which it is addressed.

This Court's nineteenth-century Commerce Clause opinions established a clear rule absolutely prohibiting state regulation of goods so long as they remained "in" interstate commerce. *E.g., Leisy v. Hardin,* 135 U.S. 100; (1890); *Bowman v. Chicago & Northwestern Ry. Co.,* 125 U.S. 465, 507-08 (1888). Thus, although the police powers of the states to regulate alcoholic beverages within their borders were firmly established, *e.g., Mugler v. Kansas,* 123 U.S. 623 (1887), *License Cases,* 46 U.S. (5 How.) 504 (1847), those powers did not extend to alcoholic beverages or any other commodities in commerce. *Leisy v. Hardin,* 135 U.S. at 119. The Court's "in commerce" rulings imposed a significant restraint on state power because of the "original package" doctrine. Under that doctrine, importation of goods was not complete until the original package in which the goods were shipped was broken or was sold. *Leisy v. Hardin,* 135 U.S. at 110.

The specific application of the original package doctrine to alcoholic beverages in *Leisy v. Hardin* led Congress to pass the Wilson Act, 27 U.S.C. § 121. The Wilson Act was designed to prevent the immunity of goods in commerce from frustrating state prohibition efforts. *See* 21 Cong. Rec. 4954 (1890) (remarks of Senator Wilson). Obviously, a local ban on alcoholic beverages would be seriously cur-

tailed so long as interstate shippers were free to import and sell them in their original packages.

The Wilson Act addressed its narrow purpose by rendering alcoholic beverages subject to state power "to the same extent and in the same manner as though" they had been produced within the state, "upon arrival" in the state. The Wilson Act removed the absolute immunity from state regulation afforded goods in commerce, but it allowed no discriminatory treatment of alcoholic beverages and offered the states no police powers they did not possess in the regulation of domestic products. *See Scott v. Donald,* 165 U.S. 58, 100 (1897) (Wilson Act did not allow discrimination against products of sister states).

The Wilson Act was soon stripped of its practical value by this Court's interpretation of the point at which goods arrived in a state. In *Rhodes v. Iowa,* 170 U.S. 412 (1898), the Court concluded that alcoholic beverages "arrived" for purposes of the Wilson Act only when they were received by the consignee. 170 U.S. at 423. Despite the Wilson Act, then, the states had no power to prevent out-of-state firms from shipping alcoholic beverages into the state. As before, the immunity of goods in commerce prevented prohibition states from preventing unwanted importation.

Congress again responded, with the passage of the Webb-Kenyon Act, 27 U.S.C. § 122. Webb-Kenyon also addressed the narrow problem of unwanted importation by forbidding the "shipment or transportation . . . of . . . intoxicating liquor of any kind, from one state . . . into any other state . . . or from any foreign country into any state" for receipt, possession, or sale in violation of state law. Webb-Kenyon thus accomplished what Wilson had not. It gave the states power to block unwanted imports at their borders. Like Wilson, Webb-Kenyon did not attempt to confer any other power. It did not address the manner in which the states might regulate alcoholic beverages once their police powers attached. This Court upheld the Webb-Kenyon Act in *Clark Distilling Co. v. Western Maryland*

Ry. Co., 242 U.S. 311 (1917), and the Court's divided ruling took on great significance in 1933 when Congress considered the repeal of the Eighteenth Amendment.[32]

The Court made clear in *Clark Distilling* Webb-Kenyon's limited purpose.

> [T]here is no room for doubt that [the Webb-Kenyon Act] was enacted simply to extend that which was done by the Wilson Act; that is to say, its purpose was to prevent the immunity characteristic of interstate commerce from being used to permit the receipt of liquor through such states contrary to their laws, and thus in effect afford a means of subterfuge and indirection to set such laws at naught.

242 U.S. at 324. No question of discrimination against commerce was involved.

As this Court recognized in *Craig v. Boren*, 429 U.S. 190 (1976), section 2 was intended to constitutionalize the state power allowed by Webb-Kenyon.

> The history of state regulation of alcoholic beverages dates from long before adoption of the Eighteenth Amendment. In the License Cases, the Court recognized a broad authority in state governments to regulate the trade of alcoholic beverages within their

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[32]*Clark Distilling* is also significant in its recognition of state police powers. Although section 2 is sometimes seen as a grant of police powers to the states, it neither was necessary as nor intended to be a grant of police powers. The police power is inherent in state sovereignty, and the police power over alcoholic beverages was acknowledged by this Court long before the Twenty-first Amendment. *E.g., Mugler v. Kansas*, 123 U.S. 623 (1887). *Clark Distilling*, which preceded the Twenty-first Amendment by sixteen years, itself sustained an exercise of state police powers over alcoholic beverages. 242 U.S. at 320.

Wilson, Webb-Kenyon and section 2 thus would be redundancies if they were meant to confer police powers. Their history shows that they were intended to allow the states to exercise a power that they did not have before—the power to regulate interstate commerce in a limited way.

> borders free from implied restrictions under the Commerce Clause. Late in the century, however, Leisy v. Hardin undercut the theoretical underpinnings of the License Cases. This led Congress, acting pursuant to its powers under the Commerce Clause, to reinvigorate the state's regulatory role through the passage of the Wilson and Webb-Kenyon Acts. . . . With passage of the Eighteenth Amendment, the uneasy tension between the Commerce Clause and state police power temporarily subsided.
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> The Twenty-first Amendment repealed the Eighteenth Amendment in 1933. The wording of § 2 of the Twenty-first Amendment closely follows the Webb-Kenyon and Wilson Acts, expressing the framers' clear intention of constitutionalizing the Commerce Clause framework established under those statutes.

429 U.S. at 205-206 (footnotes and citations omitted). That framework gave the states power to treat alcoholic beverages transported from outside the state in the same manner as they treated domestic products. It allowed nothing more.[33]

The constitutionalizing of the state power created by Webb-Kenyon was necessary in the eyes of the proponents of section 2 because of the tenuous balance created by the divided opinion in *Clark Distilling*. President Taft and Attorney General Wickersham had found Webb-Kenyon unconstitutional, and the President based his veto of the act on its asserted unconstitutionality. 76 Cong. Rec. 4170 (remarks of Senator Borah). Thus, faced with the dubious constitutionality of the act, a Court able to overrule the prior ruling in *Clark Distilling,* and Congress' ever-present power of repeal, the proponents of state power set about

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[33]Section 2 did not, of course, eliminate the Import-Export Clause prohibition of taxes on imports. *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 108 (1980).

providing constitutional status to Webb-Kenyon. The congressional debates confirm this narrow reach of section 2.

Senator Blaine was the manager of S.J. Res. 211, § 2 of which became section 2 of the Twenty-first Amendment. As such, he reported the views of the Senate Judiciary Committee to the full Senate. Senator Blaine explained the purpose of section 2 as follows:

> In the case of Clark against Maryland Railway Co. there was a divided opinion. There has been a divided opinion in respect to the earlier cases, and that division of opinion seems to have come down to a very late day. So, to assure the so-called dry states against the importation of intoxicating liquor into those states, it is proposed to write permanently into the Constitution a prohibition along that line. Mr. President, the pending proposal will give the states that guarantee . . . .

76 Cong. Rec. 4141.

Senator Borah, a member of the Senate Judiciary Committee, a participant in the earlier congressional debates on Webb-Kenyon, *see* 49 Cong. Rec. 702 (1912), and a leading opponent of the repeal of Prohibition, explained section 2 in the same way. He responded to an amendment that would have eliminated section 2 by arguing that section 2, "which provides for the protection of the so-called dry states," 76 Cong. Rec. 4170, was needed because the Webb-Kenyon Act did not provide "sufficient protection to the dry states," as it was "still of doubtful constitutionality." *Ibid.* Moreover, he argued, eliminating section 2 would mean "asking the dry states to rely upon the Congress of the United States to maintain indefinitely the Webb-Kenyon law." *Ibid.* "It does not seem to me that we can afford to strip the amendment of all effort to protect the dry States." *Ibid. See also* 76 Cong. Rec. 4219 (remarks of Senator Walsh).

The Court's Commerce Clause doctrine, the frustrations of state power it created, and the congressional efforts to ease those frustrations, all show what the debates on

section 2 confirm. The Wilson Act, the Webb-Kenyon Act, and section 2 allow the states to preclude importation of alcoholic beverages. That authorization was necessary because without it a dry state could not hope to remain dry. The articulated historical need for section 2 must be considered when its meaning is addressed.[34]

Even if the history is ignored, however, section 2 cannot be seen as an unrestricted grant of power to the states. Section 2 is limited to the prevention of unwanted "transportation or importation" into a state. That language cannot be read to justify discriminatory treatment of alcoholic beverages allowed into the state and treated, along with domestic products, as legitimate articles of commerce.

B. This Court's Opinions Establish That State Interests Must Be Subordinated to Federal Law and Policy in Appropriate Circumstances

No opinion of this Court has ever interpreted section 2 in a manner that would justify the discriminatory imposition of state taxes such as that found here. Instead, the Court has interpreted section 2 in a practical way that requires careful consideration of the "issues and interests at stake in any concrete case." *Hostetter v. Idlewild Bon*

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[34] This Court has been hesitant to consider the legislative history of section 2 in its opinions, *e.g.*, *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 106-07 n.10 (1980); *State Bd. of Equalization v. Young's Market*, 299 U.S. 59, 63-64 (1936), although the Court has noted the importation focus of section 2. *E.g.*, *Midcal*, 445 U.S. at 106-08. In *Midcal*, the Court's hesitance to examine the legislative history was attributed to canons of construction and a "reluctance to wade into the complex currents beneath the congressional proposal of the Amendment and its ratification in the state conventions." 445 U.S. at 107 n.10. In *Young's Market*, the Court rejected an effort to narrow the literal meaning of section 2 by resort to the history showing its purpose of protecting the dry states. 299 U.S. at 64. Any reliance by Hawaii on section 2 in this case would require ignoring both the language and history of section 2.

Voyage Liquor Corp., 377 U.S. 324, 332 (1964). The consideration of the issues involved in a given case must address the relationship of the asserted state interest to the core importation purpose of section 2, and avoid undue impairment of federal interests. Even when the federal power in question is based on or derived from the Commerce Clause, the constitutional provision most directly related to section 2, federal interests may overcome those asserted by the state. *E.g., California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.,* 445 U.S. 97 (1980). Moreover, state interests play a far less significant role when the central importation concern is not in issue.

The Court's earliest opinions under section 2 are sometimes said to establish a broad scope for state power under section 2. These cases, *Joseph S. Finch & Co. v. McKittrick,* 305 U.S. 395 (1939), *Indianapolis Brewing Co. v. Liquor Control Comm'n,* 305 U.S. 391 (1939), *Mahoney v. Joseph Triner Corp.,* 304 U.S. 401 (1938), and *State Bd. of Equalization v. Young's Market,* 299 U.S. 59 (1936), have not been read so broadly by this Court. Each case addressed the importation powers granted by section 2.

> This Court made clear in the early years following adoption of the Twenty-first Amendment that by virtue of its provisions a State is totally unconfined by traditional Commerce Clause limitations when it restricts the importation of intoxicants destined for use, distribution, or consumption within its borders.

Hostetter v. Idlewild Bon Voyage Liquor Corp., 377 U.S. at 330. The importation focus of the early cases again was recognized in *Midcal.*

> *Young's Market, supra,* concerned a license for interstate imports of alcohol; another case focused on a law restricting the types of liquor that could be imported from other States, *Mahoney v. Joseph Triner Corp.,* 304 U.S. 401 (1938); two others involved "retaliation" statutes barring imports from States that proscribed

> shipments of liquor from other States, *Joseph S. Finch & Co. v. McKittrick*, 305 U.S. 395 (1939); *Indianapolis Brewing Co. v. Liquor Control Comm'n*, 305 U.S. 391 (1939).

445 U.S. at 107-08. These cases, the Court stated, were decided "largely on the basis of the States' special power over the 'importation and transportation' of intoxicating liquors." 445 U.S. at 108. They did not recognize any general, preeminent state power over alcoholic beverages.

Nor has the Court interpreted its initial Twenty-First Amendment decisions as subordinating the federal commerce power to the state interests recognized by section 2.

> To draw a conclusion from this line of decisions that the Twenty-first Amendment has somehow operated to "repeal" the Commerce Clause wherever regulation of intoxicating liquors is concerned would, however, be an absurd oversimplification. If the Commerce Clause had been *pro tanto* "repealed" then Congress would be left with no regulatory power over interstate or foreign commerce in intoxicating liquor. Such a conclusion would be patently bizarre and is demonstrably incorrect.

Idlewild, 377 U.S. at 331-32.

The early cases themselves rejected the contention that section 2 eviscerated all federal power over alcoholic beverages:

> Yet even when the States had acted under the explicit terms of the Amendment, the Court resisted the contention that § 2 'freed the States from all restrictions upon the police power to be found in other provisions of the Constitution.' *Young's Market, supra*, at 64.

Midcal, 445 U.S. at 108. Thus, *Midcal* recognized that even the early, most expansive readings of section 2 do not allow state law to override federal policy simply because state law regulates alcoholic beverages.

The Court's opinions have not adopted any hard and fast rule to identify the scope of the respective federal and state powers. Instead, the Court has required that the Twenty-first Amendment and the Commerce Clause be read and considered together and the issues presented by the competing interests they represent addressed in a practical way.

> Both the Twenty-first Amendment and the Commerce Clause are parts of the same Constitution. Like other provisions of the Constitution, each must be considered in the light of the other, and in the context of the issues and interests at stake in any concrete case.

Idlewild, 377 U.S. at 331-32. *See also Joseph E. Seagram & Sons, Inc. v. Hostetter*, 384 U.S. 35 (1966). Thus, any suggestion of "absolute" state power over alcoholic beverages has been rejected by the Court.

Consistent with *Idlewild's* directive that Commerce Clause interests be considered along with those presented by section 2, the Court has abandoned the view of the early cases that other provisions of the Constitution are overridden by the Twenty-first Amendment. *Young's Market* stated in dictum that the Equal Protection Clause was irrelevant in the case of alcoholic beverages because a classification allowed by the Twenty-first Amendment could not be forbidden by the Fourteenth. *Mahoney v. Joseph Triner Corp.* followed this dictum in an opinion addressed solely to an equal protection argument. This Court's Fourteenth Amendment opinions in *Craig v. Boren*, 429 U.S. 190, 204-10 (1976) (equal protection) and *Wisconsin v. Constantineau*, 400 U.S. 433, 436 (1971) (due process) rejected these contradictions of *Idlewild's* teaching on the coexistence of these different provisions of the "same Constitution." Both cases held Fourteenth Amendment concerns to prevail over state interests asserted under the Twenty-first Amendment. *See Midcal*, 445 U.S. at 108. They showed both the Court's

rejection of the broad implications of the early cases and any rule of state preeminence.[35]

C. In the Context of the "Issues and Interest at Stake" in this Case, the Twenty-first Amendment Provides No Basis for Upholding Hawaii's Discriminatory Tax

Hawaii has not relied on the Twenty-first Amendment in attempting to justify the tax involved here. The state's failure to do so reflects the absence of any legitimate state interest to assert against the undisputed federal interest in free trade that has led to the rule discussed above establishing a "virtual" *per se* prohibition on discriminatory state taxes. Hawaii can articulate no legitimate state interest because the tax is based solely on the forbidden purpose of fostering local industry at the expense of foreign and interstate commerce. This state purpose carries no weight in the accommodation of the interests presented by this case.

As in *Midcal,* the state court has provided an identification of the state policies alleged to be served by the statute in question. Not only has the highest state court identified and articulated the protectionist goal of the statute, AJS at A-12 to A-13, the state attorney general, R. 268,[36] and the state legislature, in a specific policy statement, also have explained that the statute before the Court is based on a goal that is in no way connected with any of the concerns that led to the enactment of section 2 and one that is

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[35]For the reasons enunciated in *Craig* and *Constantineau,* the Twenty-first Amendment does not foreclose Fourteenth Amendment equal protection review of the discrimination involved here.

[36]In *Midcal,* the Court noted that the intervenor and *amicus* state attorney general failed to identify state interests in the resale price maintenance scheme other than those articulated by the state courts. 445 U.S. at 111 n.12. Here, the attorney general not only identifies no additional interests, he affirmatively asserts the purpose stated by the legislature and articulated by the Hawaii Supreme Court.

prohibited to the states by well-established Commerce Clause jurisprudence. There is no question of restricting the importation of alcoholic beverages, and nothing at all related even to traditional state police power interests in the regulation of alcoholic beverages. Instead, the Hawaii tax is designed only to promote local industry over out-of-state industry, a concern nowhere addressed by the language or history of section 2 or this Court's rulings on state power to regulate alcoholic beverages.

In *Midcal*, the state courts' articulation of the state interests and their assessment of the usefulness of the challenged state law in obtaining concededly appropriate local goals were accepted by the Court. 445 U.S. at 111-114. In this case, the state has also provided an articulation of the local interest. Because that interest is not permissible under section 2 or the Commerce Clause, this case presents no true conflict between federal and state interests, and no need to accommodate competing concerns. All that it requires is recognition of the force of the federal interest in the free flow of commerce among the states.[17]

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[17]As did *Midcal*, this case presents a clear and fundamental federal interest. In *Midcal*, the Sherman Act prohibition against price fixing provided a specific measure of the federal interest. Here also the federal interest is specific and clearly defined in this Court's decisions barring discriminatory state taxes. The case thus does not present any issue regarding the weight to be given more general federal policies.

CONCLUSION

Hawaii's discriminatory liquor tax violates basic principles of federalism. The decision of the Hawaii Supreme Court upholding the tax is contrary to these principles as consistently applied by this Court. For this reason, and the other reasons set forth in this brief, the judgment below should be reversed.

Respectfully submitted,

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